KILPATRICK TOWNSEND

5 KEY TAKEAWAYS

IP Considerations in M&A Transactions

The importance of intellectual property ("IP") in M&A transactions continues to grow as IP, technology, and data have become key components in the valuation of a business. The strength and enforceability of the target company's IP is core to the economic value of the deal and the success of the transaction. IP assets present unique challenges in M&A transactions, however, due to their highly indivisible nature.

1

From the outset of the transaction, it is important to understand the competing interests of the parties with respect to the IP assets in scope for the transaction. The seller will want to avoid:

- Assuming risk for inherent, unknown IP issues (e.g., freedom to operate, validity, and enforceability of IP);
- Encumbering IP assets that are excluded from the transaction; and
- Making assurances for IP licensed from a third-party that are not within the seller's control.

The buyer, on the other hand, will be concerned with:

- acquiring exclusive, unencumbered, and marketable title to all of the IP and technology necessary to conduct the divested business and exploit the IP assets;
- minimizing IP risks (e.g., ownership, validity, infringement of third-party IP); and
- the ability to integrate and operate the divested business and IP assets post-closing.

2

To minimize the risk inherent with IP assets, it is fundamental to understand the difference, and clearly distinguish in the transaction documents, between intellectual property rights versus technology. IP rights are purely legal rights which are intangible assets (e.g., patents, trademarks, copyrights, trade secrets), whereas technology is the embodiment of such rights in the form of tangible assets (e.g., software, know-how, algorithms)

3

Extensive IP due diligence is necessary to evaluate the economic value and strength of the IP assets to be acquired. IP portfolio analysis is complex, however, requiring IP and technology subject matter experts to investigate the IP assets included within the transaction, as well as those necessary to conduct the business being acquired. It is crucial to detect not only present issues with respect to the target IP assets, but also potential problems that might arise post-closing.

4

Key due diligence considerations center on the validity, ownership, exclusivity, and protection of the IP. Issues, risks, and potential show-stoppers include:

- third party claim that patents are invalid (e.g., due "prior art");
- third party claims that the IP infringes their rights;
- lack of documentation with respect to necessary assignments of rights by employees/contractors/third parties that contributed to the creation of the IP;
- encumbrances on the IP – security interests, liens, escrow agreements, and springing licenses;
- use of restrictive open source licenses in the IP developed or acquired by the seller; and
- violations of the seller's policies, practices, and security measures with respect to data protection and privacy issues.

5

To mitigate inherent IP risks (i.e., non-infringement) and address issues identified during due diligence, the parties will heavily negotiate the following:

- the scope of, and appropriate limitations on (i.e., materiality and knowledge qualifiers) the IP representations and warranties (e.g., ownership and title to IP assets, sufficiency of IP assets, and the validity, enforceability, and maintenance of IP assets);
- indemnities for breach of the IP representations and warranties, including the survival period for IP claims, caps on exposure, claims not limited by the cap or that have a super-cap, holdback of a portion of the purchase price that the buyer can use to set off against any losses, and control of the defense of indemnity claims;
- IP covenants that the seller must satisfy by closing (e.g., execution and/or recordation of assignments, obtaining necessary third party consents, etc.); and
- ancillary IP related agreements (e.g., post-closing license to IP assets retained by the seller that are used in conducting the divested business, transitional trademark license in order for the buyer to effectuate the change in corporate identify, etc.).

If an issue cannot be addressed pre-closing or mitigated with indemnity, the buyer should consider a reduction in the purchase price to off-set the risk assumed and the cost to remedy such risk post-closing.

For more, please contact Kilpatrick Townsend's Michelle Tyde: mtyde@kilpatricktownsend.com.